

Message Text

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ACTION EUR-12

INFO OCT-01 ISO-00 AID-05 CIAE-00 COME-00 EB-08 FRB-01
INR-10 NSAE-00 ICA-20 TRSE-00 XMB-04 OPIC-06
SP-02 LAB-04 SIL-01 OMB-01 NSC-05 SS-15 STR-07
CEA-01 AGRE-00 /103 W
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P 032300Z AUG 78
FM AMEMBASSY OTTAWA
TO SECSTATE WASHDC PRIORITY 8280
INFO ALL CONGENS IN CANADA POUCH

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PASS TREASURY FOR SYVRUD

E.O. 11652: N/A
TAGS: EFIN, ECON, CA
SUBJECT: ECONOMIC DEVELOPMENTS; WEEK ENDING JULY 28

1. SUMMARY. CANADIAN DOLLAR EXPERIENCED SHARP DOWNWARD PRESSURE FOLLOWING ANNOUNCEMENT OF JUNE TRADE DEFICIT. INVESTMENT INTENTION SURVEY SHOWS SOME IMPROVEMENT FOR 1978, BUT PRIVATE INVESTMENT WILL STILL SHOW NO REAL GROWTH FOR YEAR. INDEX OF REAL DOMESTIC PRODUCTION DECLINED 0.2 PERCENT IN MAY, WHILE INDUSTRIAL PRODUCTION DECLINED 0.8 PERCENT, SUGGESTING SECOND QUARTER GROWTH WILL NOT BE STRONG. END SUMMARY.

2. MERCHANDISE TRADE FIGURES FOR JUNE RELEASED JULY 28 SHOWED DEFICIT OF CDOLS 93 MILLION (SA, BOP BASIS) DOWN FROM SURPLUS OF CDOLS 309 MILLION (REVISED) IN MAY. JUNE WAS FIRST MONTHLY TRADE DEFICIT SINCE NOVEMBER, 1976. FOR FIRST HALF OF 1978 TRADE SURPLUS WAS AT ANNUAL RATE OF CDOLS 3.7 BILLION, DOWN FROM VIGOROUS FIRST QUARTER ANNUAL RATE OF NEARLY CDOLS 6 BILLION. JUNE TRADE FIGURES WERE AFFECTED BY SOME SPECIAL FACTORS, SUCH AS STRIKE
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(SINCE SETTLED) IN IRON MINING. WHILE MONTHLY TRADE SURPLUSES WILL RESUME, WE BELIEVE PERIOD OF ALMOST STEADY INCREASES IN MERCHANDISE TRADE SURPLUS SINCE 1976 IS NOW OVER.

3. JUNE TRADE DEFICIT LED TO SHARP DOWNWARD PRESSURE ON CANADIAN DOLLAR, DESPITE INCREASES IN BANK RATE TO 9 PER-

CENT ON JULY 25. SINCE EARLY JUNE EXCHANGE RATE HAS HOVERED NEAR 89 U.S. CENTS, BUT RATE SLID RAPIDLY DOWN NEAR 88 U.S. CENTS JULY 28 DESPITE REPORTS OF INTERVENTION TO HELP SUPPORT RATE BY BANK OF CANADA. RATE HAS SINCE SLIPPED FURTHER BELOW 88 CENTS. IN RETROSPECT, MARKET TRADERS BELIEVED BANK OF CANADA KNEW IN ADVANCE OF BAD TRADE FIGURES WHEN IT DECIDED TO RAISE BANK RATE. GOVERNOR BOUEY HAS DENIED THIS, SAYING RATE WAS INCREASED ONLY BECAUSE OF NARROWING INTEREST DIFFERENTIALS WITH U.S. BOUEY DESCRIBED FOREX MARKET REACTION TO BANK RATE INCREASE AS "PERVERSE".

4. STATCAN MID-YEAR REVIEW OF INVESTMENT INTENTIONS SHOWS SLIGHT IMPROVEMENT IN INVESTMENT OUTLOOK FOR 1978 COMPARED WITH RESULTS OF MARCH SURVEY. STATCAN NOW EXPECTS TOTAL PUBLIC AND PRIVATE INVESTMENT IN 1978 TO TOTAL CDOLS 50 BILLION, A RISE OF 7.4 PERCENT FROM 1977 LEVEL. MARCH SURVEY PROJECTED RISE OF 5.3 PERCENT IN 1978. AS PRICES OF CAPITAL GOODS ARE EXPECTED TO RISE BY 7.5 - 8 PERCENT, LATEST SURVEY IMPLIES THAT REAL INVESTMENT SPENDING WILL BE FLAT THIS YEAR -- NO GREAT SHAKES, BUT AN IMPROVEMENT OVER 2 PERCENT REAL DECLINE IMPLIED BY MARCH SURVEY.

5. MAIN UPWARD REVISIONS FROM MARCH SURVEY WERE IN AGRICULTURAL INVESTMENT (WHERE BRIGHTER OUTLOOK PROBABLY LINKED TO RENEWED GROWTH OF FARM INCOMES) AND IN UTILITIES, UNCLASSIFIED

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WHOSE REAL SPENDING COULD RISE BY 9 - 9.5 PERCENT IN 1978.

6. FOLLOWING IN BREAKDOWN OF EXPECTED CHANGES IN MAJOR CATEGORIES OF INVESTMENT SPENDING (MARCH PROJECTIONS ARE IN PARENTHESES): TOTAL PRIVATE, 10.3 PERCENT (7.4 PERCENT); PUBLIC INVESTMENT, 7.9 PERCENT (4 PERCENT); MANUFACTURING, 8.3 PERCENT (4.8 PERCENT); MINING, -5.3 PERCENT (-6.5 PERCENT); OIL AND GAS, 4.3 PERCENT (3.3 PERCENT); MACHINERY AND EQUIPMENT, 9.6 PERCENT (5.2 PERCENT); NON-RESIDENTIAL CONSTRUCTION, 9.8 PERCENT (6.4 PERCENT); RESIDENTIAL CONSTRUCTION (ASSUMES 230,000 HOUSING STARTS) 0.1 PERCENT (3.8 PERCENT).

7. COMMENT: IN VIEW OF INCREASING MARGIN OF SPARE PRODUCTIVE CAPACITY AND SLUGGISH PRODUCTION TRENDS (SEE BELOW) THE UPWARD REVISIONS ON PROJECTIONS FOR NON-RESIDENTIAL CONSTRUCTION (I.E., EXPECTED EXPANSION OF PLANT CAPACITY) IS SOMEWHAT SURPRISING.

8. INDEX OF REAL DOMESTIC PRODUCT (RDP) SEASONALLY ADJUSTED (SA), DECLINED BY 0.2 PERCENT TO 132.1 (1971 EQUALS 100) IN MAY AND STOOD 2.9 PERCENT OVER LEVEL OF MAY, 1977. AS

HAS BEEN THE CASE FOR SEVERAL MONTHS, OVERALL DROP IN INDEX AS INFLUENCED BY SHARP (7.7 PERCENT) FALL IN MINING OUTPUT. HOWEVER, MANUFACTURING OUTPUT, WHICH HAD RISEN BY 5.3 PERCENT BETWEEN JANUARY AND APRIL, FELL BY 2 PERCENT IN MAY.

9. INDEX OF INDUSTRIAL PRODUCTION (SA) DECLINED BY 0.8 PERCENT TO 178.9 (1971 EQUALS 100) IN MAY. INDEX IS 3.6 PERCENT ABOVE LEVEL OF MAY, 1977. MANUFACTURING OUTPUT DROPPED BY 2 PERCENT. WITHIN MANUFACTURING, PRODUCTION OF DURABLES WAS FLAT IN MAY WHILE NON-DURABLES OUTPUT FELL. SIGNIFICANT DECLINES REGISTERED IN

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ELECTRICAL PRODUCTS (-2.2 PERCENT), COAL AND PETROLEUM (-2.8 PERCENT) AND CHEMICALS (-3.3 PERCENT). SECTORS SHOWING IMPORTANT INCREASES WERE LEATHER (1.4 PERCENT) AND TEXTILES (1.2 PERCENT).

10. COMMENT: RDP AND INDUSTRIAL PRODUCTION WERE STRONG IN FIRST QUARTER, GROWING AT SEASONALLY ADJUSTED ANNUAL RATES OF 7.2 PERCENT AND 8.6 PERCENT RESPECTIVELY. HOWEVER, FOLLOWING LARGE INCREASES IN FEBRUARY, MONTHLY GROWTH OF INDICES HAS DECELERATED SUBSTANTIALLY. OUTPUT GROWTH IN SECOND QUARTER WILL BE UNIMPRESSIVE, AND AUGURS ILL FOR PATH OF REAL GNP.

11. WHOLESALE PRICE INDEX ROSE 0.1 PERCENT IN MAY TO 600.6 FROM REVISED APRIL LEVEL OF 600.0. WPI IN MAY WAS 7.0 PERCENT ABOVE YEAR EARLIER.

12. NEW ORDERS IN MANUFACTURING (SA) DECLINED BY 1.1 PERCENT TO CDOLS 10.7 BILLION IN MAY. DECLINE ATTRIBUTABLE TO DROP OF 3.5 PERCENT IN ORDERS FOR DURABLE GOODS, WHILE NON-DURABLE ORDERS WERE UP BY 1.1 PERCENT. VALUE OF MANUFACTURING SHIPMENTS WAS CDOLS 10.4 BILLION IN MAY, A RISE OF 0.2 PERCENT FROM APRIL; DURABLE SHIPMENTS WERE UNCLASSIFIED

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DOWN. UNFILLED ORDERS, AT CDOLS 11.5 BILLION, WERE UP 1.8 PERCENT FROM APRIL. RATIO OF OWNED INVENTORIES TO SHIPMENTS WAS 1:86 COMPARED WITH 1:85 IN APRIL. (NOTE: BEGINNING IN MAY, ORDERS/SHIPMENTS/INVENTORIES SERIES FROM JANUARY, 1975 TO MAY, 1978, ARE BASED ON 1975 CENSUS DATA RATHER THAN ON 1971 DATA, AND ARE NOT DIRECTLY COMPARABLE TO EARLIER DATA.)

13. STATCAN SURVEY OF BUSINESSMEN'S EXPECTATIONS FOR THIRD QUARTER SHOWS LESS OPTIMISM THAN EXPECTATIONS FOR SECOND QUARTER, BUT IMPROVEMENT OVER EXPECTATIONS FOR THIRD QUARTER, 1977.

14. LABOR INCOME (SA) WAS CDOLS 10.8 BILLION IN MAY, AN INCREASE OF 0.8 PERCENT FROM APRIL AND OF 9.2 PERCENT FROM MAY, 1977. AS TWELVE MONTH RISE IN CONSUMER PRICES WAS 9 PERCENT IN MAY, YEAR OVER YEAR GROWTH OF REAL LABOR INCOME WAS VIRTUALLY STAGNANT IN MAY. MOREOVER, GROWTH OF TOTAL LABOR INCOME INFLUENCED BY 2.8 PERCENT GROWTH IN EMPLOYMENT IN YEAR ENDING MAY. THUS, NOMINAL PER CAPITA EARNINGS WERE UP ONLY ABOUT 6 PERCENT OVER THIS PERIOD AND DECLINED IN REAL TERMS. ENDERS

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